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IN THE

Supreme Court of the United States

October Term, 1939.

No. 38

HOWARD S. PALMER, JAMES LEE LOOMIS and HENRY B. SAWYER, Trustees of the Property of The New York, New Haven and Hartford Railroad Company, Debtor,

Petitioners,

—against—

CONNECTICUT RAILWAY & LIGHTING COMPANY,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

Petition for Writ of Certiorari to the Circuit Court of Appeals for the Second Circuit.

JAMES GARFIELD,
HOUSTON J. WARE,
Attorneys for Petitioners.

March 25, 1940.

Rand Corporation, Washington, D. C.

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OTHER AUTHORITIES CITED:

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PETITION FOR WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

To the Honorable Chief Justice of the United States and Associate Justices of the Supreme Court of the United States:

The undersigned on behalf of the above-named petitioners pray that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit entered on February 13, 1940 reversing the decision of the District Court of the United States for the District of Connecticut.

Opinions Below.

The opinions of the courts below have not yet been officially reported. They will be found at pages 265-290 and pages 293-301 of the Record.

Jurisdiction.

The order for mandate was entered on March 2, 1940. Jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925, and Section 25(c) of the Bankruptcy Act as amended.

Questions Presented.

In adjudicating a landlord's claim for damages for rejection of a lease in the reorganization of a railroad under Section 77 of the Bankruptcy Act, as interpreted by this Court in *Connecticut Railway & Lighting Company* v. *Palmer* (305 U. S. 493), may the Circuit Court of Appeals properly

(1) allow damages on the basis of evidence which the trial court has expressly held inadequate to establish future rental value?

(2) allow damages for a portion of the unexpired term of the lease and disregard the balance of the term?

Statute Involved.

The statute involved is Section 77 of the Bankruptcy Act (11 U. S. C. A., Section 205), the pertinent provision of which is,

> "* * * In case an executory contract or unexpired lease of property shall be rejected, * * * any person injured by such * * * rejection shall for all purposes of this section be deemed to be a creditor of the debtor to the extent of the

actual damage or injury determined in accordance with principles obtaining in equity proceedings * * *."

Statement.

In 1906 the respondent leased to the predecessor of The New York, New Haven and Hartford Railroad Company certain street railway property in several towns in Connecticut for 999 years (R. 5-30, 265). On October 23, 1935 the New Haven filed a petition for reorganization under Section 77 of the Bankruptcy Act (R. 1). The petitioners are the trustees of its property appointed by the Bankruptcy Court. On December 18, 1935 the trustees rejected the lease (R. 266) and on November 16, 1935, respondent repossessed its properties (R. 268). Respondent duly filed a proof of various claims including one for damages for rejection of the lease (R. 266). On that claim the lower courts held respondent entitled to recover the difference between the rent reserved and the earnings of the property from rejection until final hearing. This Court on certiorari reversed the lower courts' decisions and remanded the case to the District Court

> "for further proceedings in accordance with the order and opinion of the Circuit Court of Appeals as herein modified and of this Court." (*Connecticut Railway & Lighting Co.* v. *Palmer*, 305 U. S. 493, 506.)

Further hearings were held before the District Court in March, 1939 (R. 3). On June 21, 1939, that court rendered a decision (R. 265-290) and on September 13, 1939 entered an order (R. 54-55) in

which it disallowed the entire claim for damages for rejection of the lease on the ground that the respondent had failed to prove damages in the manner required by the opinion of this Court.*

Respondent again appealed and the appeal was argued on January 23, 1940 (R. 293). The Circuit Court of Appeals on February 13, 1940, reversed the decision of the District Court and allowed damages for rejection of the lease in the amount of $4,411,837.61 (R. 293-301).

Specification of Errors.

The Circuit Court of Appeals erred:

1. In awarding damages on evidence expressly held by the trial court to be "inadequate" and "unsuitable" to prove them.

2. In awarding damages for a portion of the unexpired term of the lease and disregarding the balance thereof.

Reason for Granting the Writ.

The Circuit Court of Appeals "decided a federal question in a way probably in conflict with applicable decisions of this court" when it allowed damages under Section 77 of the Bankruptcy Act on the basis of evidence which failed to meet the requirements of that Section as interpreted by this Court and in a measure different from that which this Court has held is prescribed therein.

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* The only other issue at the second trial before the District Court arose out of the lease covenant to pay taxes. The decision on that matter was affirmed by the Circuit Court of Appeals and is not now questioned.

I.

The Character of the Evidence.

This Court said:

> "* * * only those damages susceptible of definite proof should be allowed" (305 U. S., p. 502).
>
> "The difficulties of proof are well recognized * * *. 'Testimony as to present rental value * * * partakes largely of the character of prophecy' * * *" (305 U. S., pp. 504, 5).
>
> "Judges in equitable proceedings will have the advantage of evidence in applying the usual rules as to the measure of damages. It is well understood that such evidence must show damages to reasonable certainty. Mere 'plausible anticipation' does not merit consideration nor are flights into the realm of pure speculation entitled to be treated as evidence. The determination of the amount to be allowed as the damage will be based on evidence which satisfies the mind" (305 U. S., p. 505).

Respondent completely failed to comply with this admonition as to the character of the evidence required to justify allowance of damages for loss of future rents. It made no attempt to show the probable rental value of the demised property. It did not even seek the opinion of any one familiar with the street railway business as to what its property would be likely to be worth. Its counsel said:

> "The past is the only criterion of the future that there is; and the production of experts to relieve one from the pains of thought in this regard is not really useful" (R. 276).

Even as to "the past" its showing was limited to earnings of the property for several recent periods which its counsel admitted were unduly brief or were "perturbed by irrelevant or inaccurate factors", and which the District Court held were "inadequate as a base for finding future rental value", "unsuitable for use as experience periods", "irrelevant", "speculative", "not even 'plausible anticipation'" (R. 273-5).

The record being thus lacking in "evidence which satisfies the mind", the court denied recovery for failure of proof.*

Respondent's attitude as exhibited at the second trial before the District Court seemed to indicate that it did not believe this Court meant what it said regarding the character of evidence required to prove damages. Its counsel said that:

> "The nervous remarks about reasonable certainty in the opinion of the Supreme Court indicate that they have no confidence that it is possible to produce evidence which will justify the award of damages based on the entire unexpired balance of the term" (R. 277-278).

His so-called evidence was submitted on the theory that the Trial Judge as "the trier of fact" would have to select, without the benefit of any evidence as to the

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* "In such a state of the record I cannot even embark upon the journey of assessment" (R. 275).

"* * *. some such survey (by an expert) might have constituted a firmer base than anything contained in the record" (R. 277).

"the evidence of claimant and debtor alike lacks that 'reasonable certainty * * * which satisfies the mind,' which is the standard of proof required under the Supreme Court opinion" (R. 282).

future, what past earnings would seem to him most likely to represent future conditions and to decide how far into the future it would be proper to project those earnings.

> "I propose to submit a whole series of ratios and a whole series of periods, so that the court can choose whatever he wants, whatever he thinks fair." (R. 109).

And again,

> "I am not making forecasts. I am leaving it to the Court to make them" (R. 139).

In other words, respondent assumed the question at issue, namely, that it had been damaged and left it to the Court as to a jury to figure out the amount of the damage. Small wonder that the Court held that there was a failure of proof of damages.

This finding of failure of proof was not directed only to damages for the entire unexpired term. It applied equally to *any* future period. Respondent had asked the court to allow recovery for any number of years up to forty or fifty. In disallowing damages the court said:

> "I hold, however, that even if claimant had been able to prove such a history or prospect of earnings for the demised premises as would support an assessment of damages for an unexpired term of, say, forty years that proof standing alone would not necessarily be adequate to support an assessment for the unexpired term of 969 years * * *" (R. 277).

The inference is clear. The proof was insufficient to establish a loss for any term, whether 969 years or forty or any other.

The Circuit Court of Appeals completely disregarded the trial judge's findings as to the inadequacy of the evidence to establish any future loss. It treated his decision as though the refusal to split the unexpired term necessarily vitiated the disallowance of damages and made immaterial the findings as to failure of proof.

We shall discuss hereinafter the ruling of the Circuit Court of Appeals that the lease might be treated as though it had been for a different period from that for which the parties made it. Here we wish to point out that even if that could properly be done the record *in this case* fails to prove damages for *any* future period. Disregarding a portion of the future term will not save respondent because it did not prove damages for any part of that term.

In discussing the proof the Circuit Court of Appeals called the trial judge "unduly critical" of respondent's evidence (R. 299), and itself selected from among the several bases which the lower court had held "inadequate" that which in its judgment "furnished a more reliable indication of future earnings than any of the others" (R. 299). This basis it found "had the great merit of covering ups as well as downs in general economic conditions", although admittedly it "included some years when a large part of the system was operated by trolleys" (R. 299). The evidence thus adopted by the Circuit Court of Appeals is the same evidence which the District Court called "unsuitable", "irrelevant", and "speculative" (R. 274).

This Court required that damages should not be awarded except on the basis of "evidence which satisfies the mind". Clearly, it is the mind of the trial court rather than the mind of the Appellate Court to

which this Court referred. If there is a difference of opinion the Court which saw the witnesses and heard their testimony and which had the entire record presented to it is the court whose mind must be satisfied. We respectfully submit that the Circuit Court of Appeals misinterpreted this Court's opinion in substituting its judgment as to the adequacy of the evidence for that of the District Court.

II.

As to the Measure of Damages.

This Court said:

> "* * * the measure (is) the present value of the rent reserved less the present rental value of the remainder of the term * * *. Here there is a remainder of 969 years" (305 U. S. pp. 504-505).

The District Court construed that language to mean that

> "* * * the unexpired term of 969 years * * * is the only term with which we are here concerned" (R. 277),

and that the

> "* * * cause of action * * * was indivisible and comprehended damages for the entire unexpired term" (R. 287).

The Circuit Court of Appeals disagreed. That respondent showed that it had lost money during the three years from rejection to hearing, that the earnings of the property had for some years been less than the rent, and that the New Haven Trustees had "lost

no time in disclaiming the lease as unprofitable" were taken as proof that "the agreed rent will continue for some years to exceed the earnings of the property". Because "the uncertainties in the way of appraising earnings in the more distant years" were considered too great, it was held that damages may be awarded for the first few years when "we are reasonably sure that the agreed rent will * * * exceed the earnings of the property" and "the unpredictable stretch beyond is disregarded" (R. 297-8).*

In this we submit the Circuit Court of Appeals erred. The question whether a landlord will be injured by rejection of his lease depends not only on what happens during the first few years after rejection, but on the entire balance of the term. It is quite conceivable, as the District Court pointed out (R. 278-9), that respondent may in the future actually make more money out of its property under bus operation than it would have received as rent under the lease to the New Haven. To assume that it has been injured by the rejection necessarily assumes that earnings will be less than the rent for the entire period. Instead of requiring proof of "actual damage or injury" as required by the statute the Circuit Court of Appeals holds that possible offsetting profits in the future may be disregarded and present loss may be assumed to measure ultimate injury. To permit re-

* The only authority cited for such disregard of part of the term is *Old Colony Railroad Co.* v. *New York, New Haven & Hartford Railroad Co.*, 98 F. (2d) 670, 672, which case was reversed by this Court in *Palmer* v. *Palmer* (305 U. S. 578), and remanded to the District Court for further proceedings in conformity with the opinion of this Court in the *Connecticut Railway & Lighting Company* case. And the reasoning of Judge Patterson, who wrote the present opinion, is inconsistent with that of the same Judge in 1932, *In re Wise Shoes, Inc.*, 2 F. Supp. 521, affirmed without opinion 64 F. (2d) 1023 (Judges Learned Hand, Augustus Hand and Swan).

covery for the 11 years after rejection and disregard the balance of the term would be to treat the lease as though it had originally been made for 40 years (1906 to 1946) instead of for 999 years. We submit that the courts have no power to remake contracts for the parties in this manner, and that this Court's opinion does not warrant such an interpretation.

This Court called attention to the difficulties of proving damages in the case of long-term leases. Commenting on its decision in *Kuehner* v. *Irving Trust Company* (299 U. S. 445), it said

> "the uncertainty as to the loss entailed by abrogation of leases * * * (grows) greater as the remainder of the term lengthens."

It pointed out that in that case the remainder was 14 years; here it is 969 years; there the lease was of a store in New York City; here "evidence of the value of unexpired terms of street railway leases would be even more difficult to produce, as possible lessees are limited in number". It referred to the added difficulty of prophesying rental value for the remainder of the term under the subnormal business conditions wherein reorganizations usually occur. As an example of the well recognized difficulty of proving damages for rejection of leases it cited *Pennsylvania Steel Company* v. *New York City Street Railway Company* (198 Fed. 721, 759), wherein the Circuit Court of Appeals disallowed claims under 999 year leases on the ground that damages had not been established with the requisite degree of certainty (305 U. S. 504-5).

Clearly these comments and references would not have been included in its opinion if this Court had

intended to say that the uncertainty of loss in long-term leases could be eliminated by treating them as short-term leases or that the "well recognized" difficulties of proof could be overcome by ignoring them and disregarding all but the earlier portion of the term.

CONCLUSION.

Wherefore, it is respectfully submitted that the decision of the Circuit Court of Appeals should be considered by this Court in the light of its opinion in Connecticut Railway & Lighting Co. v. Palmer, 305 U. S. 493, supra, and should be reversed.

JAMES GARFIELD,
HERMON J. WELLS,
Attorneys for Petitioners.

March 25, 1940.

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